



County of Los Angeles CHIEF ADMINISTRATIVE OFFICE

713 KENNETH HAHN HALL OF ADMINISTRATION • LOS ANGELES, CALIFORNIA 90012
(213) 974-1101
<http://cao.co.la.ca.us>

DAVID E. JANSSEN
Chief Administrative Officer

July 28, 2003

To: Supervisor Yvonne Brathwaite Burke, Chair
Supervisor Gloria Molina
Supervisor Zev Yaroslavsky
Supervisor Don Knabe
Supervisor Michael D. Antonovich

From: David E. Janssen
Chief Administrative Officer

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YVONNE BRATHWAITE BURKE
Second District

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Third District

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Fifth District

STATE BUDGET REPORT

Senate Adopts Compromise Budget

Sunday night, July 27, 2003, the Senate approved a bipartisan compromise budget on a 27 to 10 vote, with 5 Republicans providing votes to achieve the required two-thirds majority. The Senate then adopted 21 trailer bills containing language and law changes necessary to implement the budget, after which they recessed until August 18. The prevailing sentiment seemed to be it was not a budget to take pride in but one that needed to be done and the best that could be done given the circumstances. Republicans could take comfort in the fact that the budget spends \$7.3 billion less than last year's and does not include a tax increase (other than the VLF increase that was triggered administratively in June), and Democrats could find solace in the fact that some of the worst of the Governor's proposed cuts in health and social services were restored.

Given a historic State Budget deficit of \$38 billion that the Legislature has struggled with for months to reach agreement on what was expected to be an ugly, painful budget solution, the compromise is surprisingly benign. A major reason is that the budget relies heavily upon a variety of loans and fund transfers for as much as half of the solution. Nevertheless, according to the preliminary estimate of the Legislative Analyst, the structural budget problem that will reoccur next year will be approximately \$8 billion – about the same as estimated by the Governor.

The Assembly is expected to take up the budget bills as early as Monday night. There is no way to know whether there will be sufficient Republican votes to pass them, especially if some of the Democrats decline to vote for them, as happened in the Senate. There is also an effort underway by local government organizations to urge the

Assembly not to concur with the Senate version of AB 1749, the budget trailer bill that eliminates both the funding to cities and special districts for booking fees and counties' authority to collect them. A similar effort is being made to restore \$18.5 million in funding for the Rural and Small County Law Enforcement Program.

Budget Highlights

Major highlights of the Senate's budget package include:

- No new taxes (other than the VLF increase) but over half a billion dollars in new fees proposed by the Governor, as well as tuition increases of roughly 30 percent in higher education;
- Maintenance of the Proposition 98 funding guarantee for K-14 education;
- \$10.7 billion in 5-year bonds to cover the FY 2002-03 deficit, to be paid through a new half-cent dedicated sales tax that results from a complex swap of a half-cent of the existing local sales tax in return for an equal amount of property taxes shifted from schools to local governments;
- \$3.4 billion in additional borrowing through pension obligation bonds (\$1.9 billion) and tobacco settlement funds securitization (\$1.5 billion);
- \$1.1 billion in losses to local governments from an estimated \$850 million "gap" loss of VLF backfill from the delay in implementing the rate increase and \$250 million from a one-time shift of community redevelopment authority property taxes to schools; and
- A budget reserve estimated at \$2 billion.

The VLF "Loan"

On June 19, 2003, the Administration declared that the State could no longer afford to continue backfilling local governments and triggered an increase in the VLF rate as required by law. However, because of delays in making administrative changes, as well as a 60-day advance notice requirement, local governments will experience a three month loss of revenue of approximately \$852 million. (This number may in fact have changed due to the Controller's decision to make a partial VLF payment in July for June.) The budget compromise includes two features which will mitigate the impact of the gap loss, especially for counties. The first is that the amount of the foregone local revenue will be recognized as a loan to the State to be repaid by August 15, 2006. The second feature is that, for FY 2003-04 only, the percentage allocation of VLF revenue

between realignment programs and general government will be modified so that realignment funding is not reduced as a result of the gap.

Budget Assumptions

While the budget compromise appears balanced with a \$2 billion reserve, it relies upon numerous assumptions about both the budget year and the following year that are likely to test the adequacy of this year's reserve and offer ample challenges for next year's budget. Some of the budget year assumptions include \$800 million in revenue from negotiations with Indian tribes over gaming and \$1 billion (\$150 million more than the Governor proposed) from negotiating State employee compensation reductions or eliminating 16,000 positions.

Some of the assumptions for FY 2004-05 include: no State employee salary increases in FY 2004-05 (\$150 million); continued deferral of mandate reimbursement (\$170 million); no COLA's for State operations and minor local assistance programs (\$125 million); no COLA's or enrollment increase funding for higher education (\$214 million); a rate freeze at 2003 levels for Medi-Cal inpatient care rates; a limit on general fund bond sales (\$50 million); and an IHSS wage freeze (\$14 million).

Finally, in order to reduce the structural deficit in FY 2004-05, many of the savings are assumed for that year also.

Program Impacts of Interest to the County

Social Services

- Adds \$1.6 million for counties to provide transitional food stamp benefits for 5 months to former CalWORKs participants;
- Requires counties to pay 25 percent of Federal child support penalties (\$53 million) which will cost the County \$10.4 million, and creates a working group to examine equity issues related to the current State allocation to county agencies;
- Appropriates \$14 million to continue the Statewide Fingerprint Imaging System;
- Suspends the January 2004 State SSI/SSP cost of living adjustment (\$104 million); and

- Suspends the IHSS wage trigger for FY 2003-04, maintaining the maximum wage at \$9.50 per hour.

Health/Mental Health

- 5 percent rate reduction for Medi-Cal providers, effective January 1, 2004 (\$87 million); however, hospital services and federally qualified health clinics are exempt. A similar 5 percent reduction is applied to various non-Medi-Cal providers including California Childrens Services (\$943,000);
- All 34 optional Medi-Cal benefits are retained;
- In FY 2004-05, hospital inpatient rates will be frozen at 2003 levels;
- Restores Medi-Cal eligibility to aged, blind and disabled persons with income at or below the SSI/SSP level, continues expansion of the 1931(b) Program, restores the supplemental wage rate adjustment program (eliminated by SB 26X), and provides for 12 months of continuous eligibility for children in Medi-Cal;
- Imposes a 6 percent Quality Improvement Assessment Fee on certain health care providers which will be used to draw down Federal matching funds, some of which will be returned to providers as a rate increase;
- 5 percent rate reduction for Mental Health Managed Care (\$11.5 million), effective July 1, 2003;
- \$69 million in Federal funds for county mental health services for special education pupils;
- The Early Mental Health Initiative is funded at \$10 million; and
- A \$11.5 million reduction in local discretionary alcohol and drug funding.

Public Safety

- Elimination of the backfill to cities for booking fees charged by counties (\$38.2 million) and repeal of counties' authority to charge booking fees, resulting in a budgetary loss to the County of \$1.1 million;
- Elimination of High Technology Grants (\$18.5 million);

- Increases in the sliding fees charged to counties for placement of youthful offenders in the California Youth Authority (\$6 million);
- A reduction of \$16.3 million in both the Citizens' Option for Public Safety and Juvenile Justice for Crime Prevention Programs;
- Restores \$25.2 million for Peace Officers Standards and Training and eliminates Correctional Peace Officers' Standards and Training to save \$16.2 million;
- Consolidates and reduces funding by 50 percent for five vertical prosecution programs (\$8.2 million);
- Creates a court facility working group to look at the issue of court security; and
- Contains the negotiated agreement limiting the undesignated court fee transfer to \$31 million.

Transportation

- Partial suspension of Proposition 42, deferring the transfer of \$856 million, which will result in a loss in FY 2003-04 of \$188 million to cities and counties for local streets and roads.

General Government

- Reduces support to local public libraries by 50 percent to \$15.8 million, resulting in a loss of \$1.6 million to our county; and
- Eliminates \$11 million in State funding for the Arts Council, leaving \$3 million for administration only.
- In return for shifting \$250 million of property taxes to schools, community redevelopment agencies will be able to extend the time limit on the use of tax increment to repay their indebtedness by one year.

Public Resources

- Grants made from Proposition 40 funds for the purposes of the Roberti-Z'berg-Harris Open Space and Recreation Program Act appropriated prior to June 30, 2004 will no longer require a 30 percent local match.

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- \$20 million of Proposition 50 funds are allocated to the State Department of Water Resources to be used for competitive grants for groundwater management and recharge. Not more than 50 percent of the projects are to be in Northern California, and projects in Southern California are given preference if they are outside of the Metropolitan Water District's service area.

We will continue to keep you advised.

DEJ:GK
MAL:JR:lm

c: Executive Officer, Board of Supervisors
 County Counsel
 Local 660
 All Department Heads
 Legislative Strategist
 Coalition of County Unions
 California Contract Cities Association
 Independent Cities Association
 League of California Cities
 City Managers Associations